

# Procurement in WA; Government as 'model client'

Submission to the WA Commission of Inquiry into Government Programs and Projects

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Friday 21 July 2017



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*Consult Australia represents close to 300 built environment focused consulting firms, who employ approximately 45,000 employees nationally, within an industry that generates in excess of \$40 billion in revenue annually. Our firms range from some of the world's largest and most innovative companies with global expertise, through to smaller firms who are passionate about improving the area in which they operate. Consult Australia represents engineers, architects, surveyors, project managers, management consultants and more, who use their collective skill and expertise to make and shape our cities and towns into more liveable and affordable places in which to live. Beyond professions, we represent ideas and new ways of working.*



*The Association of Consulting Architects (ACA) is a national, non-profit, member-based association that leads the discussion on business matters in architecture in Australia. We are the peak body representing architectural employers and helps architectural firms navigate the changing world of practice. The ACA provide regular advice and information on business and employment matters, promote awareness of and discussion about business issues, and advocate for better business practices and legislative frameworks. The ACA (WA) Branch has a membership of over 50 practices, representing over 800 architects and design professionals. Our members include major national and international firms, and the majority of medium sized practices working in metropolitan Perth.*

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*The Australian Institute of Architects is the peak body for the architectural profession in Australia, representing 11,000 members. The Institute works to improve our built environment by promoting quality, responsible, sustainable design. It also aims to enhance the cultural, environmental and economic well-being of the community by advancing contemporary practice and the professional capability of members, and advocating the value of architecture and architects.*



*Master Builders WA's membership comprises 1950 principal contractor, subcontractor, supplier and industry consultant firms across all industry sectors. With approximately 85% of all active principal contractors and a significant proportion of subcontractors on board, Master Builder members represent a substantial part of WA's approximately 140,000 strong construction industry workforce, which is about 10% of the State workforce and employs nearly 50% of all WA's apprentices. Nationally, we are part of Master Builders Australia, a federation of nine organisations with a total membership of 33,000.*

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## RECOMMENDATIONS

The following is a summary of recommendations from this submission:

- 1) *The Inquiry should recognise those areas of procurement in Western Australia that are done well and the positive changes that have already been made in recent years.*
- 2) *As part of a new policy on 'Best Practice Procurement for Government Infrastructure', the WA Government should move away from practices that are currently based only on habit and set clear guidelines for the public sector on how to select the most appropriate procurement and delivery mechanisms for future projects and infrastructure.*
- 3) **Support the creation of a healthier procurement and risk management culture in WA by reviewing and improving the current Strategic Asset Management Framework (SAMF) and ensuring that all state government agencies and GTEs act as a 'model client' at all times.**
- 4) *The WA Government should establish an independent statutory planning authority tasked with the development and periodic review of a long term, 20 plus year, infrastructure plan for the State.*
- 5) *The WA Government, through the Office of the Auditor General, should prepare a publicly available assessment for the Inquiry on the range of contract types, terms, and variations currently used within Western Australia, including an analysis of costs, benefits and the wider impacts of these.*
- 6) **The WA Government should prohibit contracts from referencing 'unlimited liability' and promote a better understanding by all stakeholders on the limitations of liability and the need for good risk management.**
- 7) *The WA Government, through the Office of the Auditor General, should undertake an assessment of insurance as it relates to all stakeholders involved in the procurement of government infrastructure, with a particular focus on the understanding, costs and uptake of indemnity cover by professional services firms and builders.*
- 8) **As part of a new WA Government Policy on Best Practice Procurement of Government Infrastructure, set clear guidelines for the allocation of project risk.**
- 9) **The WA Government should adopt a policy of using Australian Standard 4122-2010 General Conditions of Contract for Consultants for all professional services, and Australian Standard 4000-1997/2124-1992 General Conditions of Contract for building and construction, in the State on an 'if not why not' basis.**
- 10) **The WA Government should immediately prohibit the contracting out of proportionate liability from all government contracts with professional services and building firms.**
- 11) **The Civil Liability Act 2002 must be amended to prohibit contracting out of proportionate liability for apportionable claims, notably through reform of Section 4A(1).**
- 12) *Pre-procurement consultation, including early project definition planning and business case development, should be undertaken, where appropriate, to ensure project objectives are sufficiently clear and to support innovation before any tender process begins.*
- 13) *The WA Government should establish and oversee a strategic Procurement Innovation Fund to allow them to work with specific agencies to trial more innovative ways of procuring government infrastructure without impacting negatively on project budgets and allowing for savings to be paid back into the fund.*
- 14) *As part of a new WA Government policy on Best Practice Procurement of Government Infrastructure, recognise the time, effort and costs assumed by industry in the preparation of tender documents and seek to reduce these wherever possible, and to provide compensation where appropriate to encourage competitiveness, innovation and industry sustainability.*

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- 15) *As part of a new WA Government policy on Best Practice Procurement of Government Infrastructure, recognise the need to consider 'whole of life' costs that ensure appropriate consideration for future demand, later stage expansion, alternative uses, maintenance, operational and decommissioning costs.*
- 16) *The WA Government should implement a 'two envelope' approach to tender consideration, allowing for the expertise and capacity of professional services firms and builders to be considered separately from the tender price and independent price assessment, if undertaken.*
- 17) *The WA Government should implement an agency wide 'unusually low bids' policy and ensure that such a policy is used effectively to discourage such practices from occurring.*
- 18) *The WA Government should establish a practice of setting and disclosing selection criteria and weightings for all tenders, with this information centrally collated by the WA Government for future data analysis.*
- 19) *Standard practice in Western Australia should require that firms involved in unsuccessful bids are provided with detailed feedback when requested.*
- 20) *As part of a new WA Government Policy on Best Practice Procurement of Government Infrastructure, provide guidance on when it is appropriate to consider non-confirming bids and what should occur when issues or problems are found with the tender process or project brief.*
- 21) ***The WA Government should undertake an assessment of insurance, contract and risk literacy within the public service, using this to facilitate appropriate training in conjunction with relevant professional and industry associations.***
- 22) *That care is taken to understanding and address the public-sector culture as a key component to implementing existing and future reforms in the procurement of government infrastructure in Western Australia.*
- 23) *Incorporate procurement performance indicators into the measurement of WA Government department/agency/GTE heads and senior management.*

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## 1 | EXECUTIVE SUMMARY

Consult Australia (CA), Association of Consulting Architects (ACA), Australian Institute of Architects (AIA), and the Master Builders Association (MBA) are industry associations that represent a vast array of multi-disciplinary professional services firms, individual professionals, builders and subcontractors working within the built environment. Collectively our associations represent firms and individuals that have a significant positive impact on the Western Australia economy and urban environment, including through project design, engineering, architecture, building, surveying, project management, community engagement, and planning services.

Approximately 40 per cent of our industry's work is undertaken for public sector clients, and our members have played vital roles in the creation of some of Australia's iconic public infrastructure, including road, rail, hospital, airport, educational facilities, water and energy utilities, justice, aged care, sports stadia, and urban renewal projects.

Procurement of government infrastructure is therefore an issue of particular importance to all our members, as well as the wider industry we collectively represent.

### Focus of this submission

Whilst our collective expertise and experience covers the full range of the Terms of Reference (TOR) for this Inquiry, our member firms rely heavily on optimal public sector procurement to deliver value for money and best project outcomes for their clients. As such, the decision was made to **focus solely on Item 3 of the TOR, namely the 'adequacy of their procurement processes'**, to ensure our respective organisations:

1. Do not get caught up in any potential politicisation of particular projects; and
2. Use the opportunity to highlight procurement related issues that are consistently encountered on government projects and which continue to remain as a barrier to value for money delivery to taxpayers; and
3. Provide recommendations, in a constructive manner, which if implemented in a collaborative

way with industry, should ameliorate any ongoing issues and benefit all concerned;

As such, this submission is structured in the following way to ensure that both concerns and opportunities are highlighted in the best possible way:

1. Policy;
2. Fairer Contracting;
3. Quality and Cost;
4. Evaluation and Staging; and
5. Monitor, Research and Reporting;

We are aware and hopeful that any policy reforms that arise from this Inquiry have the potential to dramatically assist our industry's operations, while also achieving better infrastructure and value for money for the people of Western Australia.

## PART I - POLICY

### Defining the procurement relationship

While every project is different to some extent, there is a significant role for the WA Government to play in setting the type of relationship that businesses in our industry have with public sector clients and also the behaviour of private sector clients.

Promoting and instilling a collaborative culture amongst public and private sector proponents in the built environment starts well before any project specific engagement. Therefore, subject to reasonable probity checks and balances, it is important that both public and private sector professionals can regularly engage and interact with each other, such as attending and participating in industry run events and best practice initiatives, so that both can maximise the shared knowledge and experience amongst each other and ultimately return best value for money to the taxpayer.

This ongoing and pre-project interaction is but one aspect of our collective call for Government to act as a 'model client'. It is this 'model client' that collectively we see as a key determinant of the efficacy of procuring government infrastructure. As the party with the greatest bargaining power, how the public-sector approaches procurement sets out the parameters of the relationship with industry, allocating risk and reward, and creating a series of incentives and disincentives for the work to be undertaken in a particular way.

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**A government that fails to act as a model client in its procurement practices is doing a major disservice to the public by supporting systemic issues associated with poor risk management and inefficient contracting. This failure places undue burdens on industry resulting in a less productive and competitive business environment, and ultimately leads to an unsustainable industry in the longer term.**

## Sub-standard practices in WA

While procurement of government infrastructure is done well in some instances, in many others there is significant scope for improvement. Addressing this in Western Australia is especially important coming off the wave of infrastructure development, limitations on industry capacity, expected population growth and the need to mitigate the negative effects of the cyclical nature of public infrastructure investment.

One of the biggest issues facing procurement in Western Australia is risk management. At present, risk is often being allocated not according to who is best able to manage it but according to bargaining power.

Professional services firms are very often the party with the least bargaining power in these transactions and typically often also the least able to absorb the insurance premiums associated with taking on disproportionate or 'unlimited' levels of risk. That assumes appropriate insurance coverage is available - at present this is possible in some cases, but is not guaranteed as local or international insurance markets inevitably tighten.

Poor risk management potentially invalidates professional indemnity insurance cover, leads to cost increases to account for the extra risk, and drives a range of behavioural responses that ultimately impact on a project's success. The consequence is systemic risks to the WA economy and reduced business confidence, translating into a significant disincentive to undertake work for certain public sector clients.

The use of standard, fair contracts negotiated between industry and government, with input from relevant stakeholders, will reduce the need for costly legal review or negotiations, and gives all parties the comfort of knowing that risk and reward is allocated fairly to help avoid some of the negative outcomes described here.

Possible causes of these inefficiencies include a loss of procurement skills from the public service and a tendency to not engage independent private sector expertise with national and international experience in this area. Instead, collectively our members see the public-sector has succumbed to a defensive, internal legally driven, risk averse approach to procurement within the State.

Finally, this has occurred within a public-sector procurement culture that discourages relevant officials from trying new ways of doing things when the existing procurement methods are perceived as adequate.

## Recognition of existing good work

This submission deals with those areas in need of improvement, but it is also important for the Inquiry to recognise those areas of procurement in Western Australia that are already done well, and the positive reforms that have been introduced in recent years.

Procurement policy can never be perfect; it is a constant balancing act between competing interests and objectives that shift with every project and as innovations bring new technologies and ways of doing things into the mix.

### *Recommendation 1*

*The Inquiry should recognise those areas of procurement in Western Australia that are done well and the positive changes that have already been made in recent years.*

## The solutions are well known

Consult Australia released two major pieces of research into procurement in 2015 concerned with the impact of sub-optimal procurement for project outcomes and value for money. Both reports contain recommendations directly relevant to the terms of reference for this Inquiry.

The first of these, *The Economic Benefits of Better Procurement*, is an economic study undertaken by Deloitte Access Economics, quantifying the potential cost savings to public sector agencies through improved procurement. It also analyses the benefits to the Australian economy, and discusses policy reforms that could lead to these benefits. *The Economic Benefits of*

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*Better Procurement* is attached to this submission as **Appendix A**.

The second report, *Better Buying, Better Outcomes*, is a qualitative study based on a series of interviews with industry representatives, together with contractors and public sector clients. It discusses areas of procurement where things are done well, and areas where different approaches may yield better results. This report is attached to this submission as **Appendix B**.

In addition, the *Western Australian Auditor General, Major Capital Projects Report 12 of October 2012*, in its key findings highlights that 'Approximately 90 per cent (\$2.953 billion) of the cost variance for projects occurred during the evaluation phase of the project when the project business case was developed and the project scope and costs were more accurately defined.'

We would encourage the Inquiry to carefully consider both Consult Australia reports, the Auditor General's report and the recommendations within the body of this submission.

Additional resources the Inquiry might find useful are contained in the bibliography to this submission.

## 2 | PROFESSIONAL SERVICES

As part of the complex web of stakeholders involved in delivering government infrastructure in Western Australia, professional service firms are vital.

These firms are responsible for the front-end work of a project, from feasibility and scoping studies, to environmental impact and corridor analysis, through to technical advice on a project's challenges, preliminary and final designs, engineering, and management at the construction phase.

While these services on average account for 19 per cent of total project value for public sector built environment projects<sup>1</sup>, the work of professional services firms greatly impacts on the final cost and quality of projects in their entirety.

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<sup>1</sup> Deloitte Access Economics, *Economic benefits of better procurement practices*, 2015, p5

<sup>2</sup> For example, Ashurst Australia with Australian Constructors Association and Infrastructure Partnerships Australia, *Scope for Improvement 2014: Project pressure points – where industry stands*, [www.constructors.com.au](http://www.constructors.com.au), 2014; and Western Australian Auditor

Indeed, it has been noted in several external reports<sup>2</sup> that greater investment in the planning and design stages of a project will yield a positive dividend to clients.

Innovations such as Building Information Modelling (BIM), which seek to front-end project decision making and potential design issues to when they can be more cost effectively dealt with, are intended to deliver on such increases in early stage investment.

## Challenges and opportunities from different project delivery methods

The means through which professional service consultants and builders are engaged can vary greatly, according to the project at hand and the delivery mechanism used to undertake the project. In seeking to improve the procurement of government infrastructure in Western Australia, it is critically important to recognise the differences and similarities between the roles of a consultant, builders and contractors.

The different delivery mechanisms used to deliver government infrastructure in Western Australia generally include:

- **Construct Only** – public sector agencies separately and directly engage the design team<sup>3</sup>, to undertake design and documentation, and contractors;
- **Design and Construct** – public sector agency engages a contractor to design, document and construct the project works, based on the agency's design brief. The contractor either uses in-house resources to prepare the design and documentation or bids as part of a consortium that includes an external design team.
- **Managing contractor** – public sector agencies engage a managing contractor, who in turn is responsible for engaging all other parties, including the design team and other

General, Major Capital Projects Report 12, <https://audit.wa.gov.au>, October 2012

<sup>3</sup> A 'Design Team' usually consists of architects, consulting engineers, and quantity surveyors, with other professional services or specialists included depending on the nature, size and type of the project.

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contractors;

- **Construction Management** – public sector agencies directly engage the design team, constructors and other service providers, while taking a project management role themselves;
- **Early Contractor Involvement** – A two stage process, whereby the public-sector agency undertakes concept design work in collaboration with private sector consultants, before a second stage resembling 'design and construct' is used to construct the project;
- **Alliance** – A new entity is formed comprised of the client and service providers, whereby risk and reward is shared and collaboration is encouraged;
- **Public Private Partnership** – A range of structures are used, but essentially a private sector project vehicle is formed to undertake the project (including using the mechanisms described above), with that vehicle then retaining a concession that may own, operate or maintain the infrastructure in return for user charges or a government payment.

For a more comprehensive discussion of each of these, including relative pros and cons, and the most appropriate circumstances to use each, we recommend that the Inquiry consider the Australasian Procurement and Construction Council's *Building and Construction Procurement Guide*, published jointly with Austroads in 2014;<sup>4</sup> and the Office of the Victorian Government Architect's 'Government as 'Smart Client'' of August 2013.<sup>5</sup>

Nevertheless, a few points need to be made about the importance of selecting the appropriate delivery mechanism, and its impact on project success.

Delivery mechanisms play a crucial role in determining risk allocation between the parties, and in turn driving or creating a disincentive for innovation, while also driving the behavior of the parties as they interact and work together to develop a project.

The other important point to be made is that because most project delivery mechanisms are ultimately a complex web of contractual relationships, project risk and reward are often allocated according to the respective levels of bargaining power, rather than with the most appropriate party.

Professional service firms are often presented with contracts treating them as though they are constructors, despite different legal standards for their work, and different models of doing business (for example, contractors generally take on a project and work to earn a profit, whereas consultants charge a fee for their service).

It is of vital importance that the appropriate delivery mechanism be used for each project, rather than sticking to a default method that might have been successful (or even partially so) in the past. In our experience, too often *Design and Construct* is used as a default delivery mechanism by public sector clients, who see the benefits offered by the service providers allocating risk between each other without taking on risk themselves – even where the public sector may be the most-suited to managing certain project risks.

In some cases, the bias towards this mechanism may be simply based on an individual or team's belief in its past success, even though that may have occurred under very different circumstances.

A better approach is for an unbiased consideration of the project's requirements and the objective use of the best suited delivery mechanism.

## Recommendation 2

*As part of a new policy on 'Best Practice Procurement for Government Infrastructure', the WA Government should move away from practices that are currently based only on habit and set clear guidelines for the public sector on how to select the most appropriate procurement and delivery mechanisms for future projects and infrastructure.*

<sup>4</sup> Australasian Procurement and Construction Council and Austroads, *Building and Construction Procurement Guide: Principles and Options*, www.apcc.gov.au, 2014

<sup>5</sup> Office of the Victorian Government Architect, 'Government as 'Smart Client''. www.ovga.vic.gov.au, 2013.

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## A poor risk management culture

The nature of contracting and project delivery has changed greatly over the past 30 years. Three decades ago, public sector clients employed more internal expertise. They were therefore better informed and experienced as organisations, with a clearer understanding of risk, a healthier appetite for risk management, and a greater ability to document and clearly define their projects.

In short, in the past risk was borne by the public sector as part of their day-to-day operations, not shunned.

With 'traditional' contracting, particularly in the public sector, risks began to manifest themselves in the form of variation claims being against the client. The extent of these claims and the response to them by the public sector indicated an intolerance of what appeared to be uncontrolled risk outcomes being borne by government. Conventional contracting has more recently, in some cases, been replaced by equity and partnership investment including Build Own Operate (BOO), Build Own Operate Transfer (BOOT) and other types of Public Private Partnership (PPP) schemes.

Public sector risk allocation policies in such schemes tend to move risk away from the government. In other cases, alliances are developed, where the risks and rewards of the project are shared.

The various relationship models for the delivery of professional consulting services generally fall into one of the following broad categories:

- (a) The firm is contracted directly to the owner as the owner's consultant for the provision of their professional services,
- (b) The firm is sub-contracted to the owner's contractor who is the client for the provision of their professional services,
- (c) The firm works in a joint venture, consortium or equity partnership with the owner or owner's contractor for the provision of their professional services, or
- (d) The firm works in joint venture partnership with another consulting firm for the provision of their professional services.

In addition, private investors now have a more 'arms length' involvement in their infrastructure investments. Large institutional financial investors (such as superannuation funds) allocate their funds to low risk and low volatility investments which means that they are unprepared to knowingly carry risk themselves.

The result of all the above changes is that there has been a shift of many project and risk responsibilities from public sector client organisations to consultants and construction companies who then contractually pass the risk on to other professional services firms and subcontractors. Part of this is based on the (often false) presumption that consultants are in particular better able to understand and therefore are most-suited to manage those risks, or simply a false presumption that consultants somehow have a stronger bargaining position than what they do.

## Systemic risk to WA Economy

Some public and private sector clients are using their market power to adopt a position that present systemic risks to the WA economy and business confidence.

In having their own assumed best interests in mind, they often believe that risk should be transferred to a construction firm or professional services firm (such as the consulting engineer or architect), even though these firms are unable to effectively manage those risks, if at all.

It is important here to highlight that technical capability and risk (e.g. is something designed correctly) is different from a firm's commercial capability to manage risk (e.g. having sufficient assets or capital).

A similar position is often adopted by the financial institutions and contractors, reinforcing a culture of inappropriate risk allocation where the burden is placed on professional services firms and contractors.

This culture can make a wide range of consultants and contractors liable for the entirety of the losses associated with the project, including in some instances economic loss which a court may not normally ascribe to professional liability.

This may have been reluctantly tolerated business practice in the past when insurance costs were moderate and availability relatively unrestricted. Today, and particularly in tougher insurance environments, this inappropriate transfer of risk drives the cost and

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availability of professional indemnity insurance beyond the capacity of some consulting firms to afford, obtain, and retain over the often long life of the liability exposure.

As a result, some professional services firms and contractors now choose to avoid government and public sector work where a poor procurement culture persists (such as the contracting out of proportionate liability described later in this submission).

In particular, Consultants whose financial benefit from projects is a fraction of that derived by the client and contractor, are the contractual party who are least able to sustain the high costs and resulting increased exposure to inappropriate uninsured liabilities. Nevertheless, they often bear an onerous share of costs and risks because they have the least bargaining power – especially when compared to the WA Government.

## Acting as a model client

Practically being a 'model client' means working collaboratively with industry on projects, and achieving mutually beneficial outcomes rather than seeking to 'beat' industry.

Being a model client in terms of procurement means that government's intent to do things better is followed through in practice, and the public sector is always looking out for better ways to do things.

The base guidelines necessary for government to act as a model client, and hence create a healthier procurement and risk management culture in WA, are already available in the form of the Strategic Asset Management Framework (SAMF). The SAMF, as referred to by the WA Auditor General on page 14 of his October 2012 report into Major Capital Projects, is the strategy to 'enable effective and efficient asset management and capital investment across the state public sector'. Whilst adherence by state government agencies and trading enterprises (GTEs) to the SAMF is mandated by Treasury, there are additional items contained within this submission which could well be adopted to improve on the current guidelines. Further improvement and subsequent adherence to the SAMF by the government agencies and GTEs should practically translate into making government a more attractive client for industry to work with, act as a positive force on business confidence, and in turn attract more and better quality tenders on projects.

In addition to processes and procedure like those outlined in the SAMF, being a model client also relates to each project and the individuals involved, with many disputes attributable to up front and behavioral factors. As such, for more information on ways the WA Government can act as a model client and avoid disputes, refer to the Cooperative Research Centre for Construction Innovation, *Guide to Leading Practice for Dispute Avoidance and Resolution*.

## Recommendation 3

*Support the creation of a healthier procurement and risk management culture in WA by reviewing and improving the current State Asset Management Framework (SAMF) and ensuring that all state government agencies and GTEs act as a 'model client' at all times.*

## 3 | INFRASTRUCTURE WA

In parallel with considering how infrastructure is procured by government in Western Australia, it is important to ensure that the procurement demands of government can be effectively met by industry.

This relates to five principal areas:

- The number and timing of projects
- Project scale, partitioning and interfacing
- Industry capability, skills and workload
- Certainty of project funding
- Long term protection of infrastructure corridors

At present, Western Australia lacks a long term (20 plus year) infrastructure plan compiled and coordinated by an independent statutory authority, like Infrastructure Victoria. The lack of such an authority tasked to provide a long term detailed plan for the State, coupled with the current complexities of processes and systems (as outlined in the Infrastructure Coalition's *Building the West* paper), directly impacts the long-term sustainability of professional services and building firms within the state.

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The previous boom evidenced how quickly the local labour market can become over heated and unable to cope due to a lack of foresight and transparent planning which would allow such businesses to adjust their resourcing requirements with greater confidence and certainty during harder economic times.

Claims that such additional human resource needs can be readily filled from interstate and overseas are only partially correct. **An infrastructure boom increases the risk that major projects will be inefficiently procured at the taxpayer's expense.**

## Building local capacity

Efforts to export professional and building services from Western Australia (often captured within terms such as the 'knowledge economy'), is dependent on local professional services and building firms having sufficient underlying work to sustain their local operations.

By using a consistent procurement pipeline to develop local capacities when funding is more readily available, Western Australia will alleviate the negative pressure placed on the professional services and building sectors during quieter periods.

## Pipeline transparency is essential

A government having a pipeline of infrastructure projects is of limited value if industry is unaware of its existence or the detail of what will be being procured over time. Limited transparency restricts the ability of firms to undertake workforce planning and reduces the incentive to invest in staff skills and capacities.

## A structure for better long term planning

This opportunity for greater long term and transparent planning in WA was somewhat missed during the recent mining boom in Western Australia. The implementation of an independent statutory planning authority, tasked with the development and periodic review of a long term, 20 plus year, infrastructure plan for WA will go a long way to avoid the current pipeline and transparency issues that the State faces.

## Recommendation 4

*The WA Government should establish an independent statutory planning authority tasked with the development and periodic review of a long term, 20 plus year, infrastructure plan for the State.*

## **PART II - FAIRER CONTRACTING**

### **4 | RISK, CONTRACTS & LIABILITY**

As we indicated in the previous part of this submission, too often project risk is allocated according to bargaining power rather than ability to manage risk.

Contracts are offered on a 'take it or leave it' basis, with little ability to negotiate around onerous terms that a service provider might not be able to meet or that places unreasonable stress on their business.

Sometimes firms may be forced to enter such unfair contracts because they are unable to walk away from a project for commercial reasons, even though it might place their business at risk, while in other situations, firms may not even be aware of the legal implications of certain contract terms, leading to reduced risk transparency.

Where this manifests in construction contracts, several undesirable outcomes may result. While public sector agencies may pass on risk under the (illusory) impression that they are protecting the taxpayer, their actions may actually serve to drive up prices, increase delays, and potentially invalidate the very insurance cover firms rely on for their protection.

At a contractual level, firms operating in Western Australia face a range of problematic issues, including but not limited to the following.

### **Excessive use of non-standard contracts and clause variations**

Firms are spending an increasing amount of unnecessary time on contract negotiation, management and litigation resulting from many projects needlessly avoiding the use of standard documents such as Australian Standard 4122-2010 General Conditions of Contract for Consultants (explored further in this

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submission) and Australian Standard 4000-1997/2124-1992 General Conditions of Contract.

## Recommendation 5

*The WA Government should prepare a publicly available assessment for the Inquiry on the range of contract types, terms, and variations currently used within Western Australia, including an analysis of costs, benefits and the wider impacts of these.*

## Onerous risk allocation through indemnities

A contractual indemnity requires one party to take responsibility for any loss that might be suffered by another party that they are indemnifying, even if that loss was caused by that other party's own actions. This can be further exacerbated through third party indemnities (discussed further later in this submission).

Generally, professional indemnity insurance will only cover consultants for loss resulting from their own acts or omissions. Broad indemnities, or those not relying on the fault of the insured party, are highly problematic because they often fail to align to actual risks or available insurance policies.

## Disproportionate allocation of liability

Under the Civil Liability Act 2002, proportionate liability allocates liability between multiple parties according to the contribution to loss made by each. However, in WA the ability to 'contract out' of proportionate liability exists, meaning that each party may be responsible for a much larger share of any loss than they were responsible for.

This issue is discussed in greater detail later in this submission.

## The illusion of unlimited liability

A contractual limit on liability set with reference to a thorough risk assessment allows business to properly insure their work and provide certainty for themselves and their clients.

*"A rigid application of unlimited contractual liability is an oppressive approach to contracting and risk allocation because it can require a consultant to place its whole business at risk for one government contract."*

Tony Horan, LLB, BA (Hons)<sup>6</sup>

As liability is always limited to a defendant's assets, and their ability to pay for any loss realised, unlimited liability is illusory and referring to it in contracts encourages poor risk management, as well as disincentivising settlement in the event of a dispute.

## Recommendation 6

*The WA Government should prohibit contracts from referencing 'unlimited liability' and promote a better understanding by all stakeholders on the limitations of liability and the need for good risk management.*

## Insurance implications

Unlike other parties involved in infrastructure development, professional services firms are generally an asset poor class of business, with a majority being small and medium enterprises. Because the service they provide is professional expertise rather than a tangible good, they depend on professional indemnity insurance to cover liability risks that arise, including contract disputes or failures in the delivery of a final product.

Indeed, consulting firms generally take out broad ranging and often expensive insurance policies to cover liabilities arising from their work, and to protect their business and personal assets. For professional services firms, professional indemnity insurance premiums are one of their largest expenses.

As a general rule, professional indemnity insurance only covers consultants for loss arising out of their errors or omissions, and where a consultant has entered into a contract that takes on risk beyond what they would be responsible for in their common-law position, insurance will typically not respond to any claim that results.

<sup>6</sup> Horan, T., *Memorandum of Advice: Uncapped liability for consultants under Guidelines for the Limitation of Liability of Suppliers, Consultants and Contractors*, 2013, 4(d)

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In situations where such a contract has been entered into, and a loss results, consultants must then meet any liabilities without insurance, from their personal assets. Where the consultant has insufficient personal assets (often the case given the asset-poor nature of most professional services firms) or have isolated them, then the loss will ultimately sit with the client – in many cases the WA Government and taxpayers.

It is particularly important to note that where a contract forces onerous risk onto a particular party, some businesses will be unaware that the contract in question might not be covered by their insurance, which in itself is an undesirable outcome.

Some parties will take the risk by undertaking the work, knowing that they're not fully insured, while other parties will deem the risk of proceeding uninsured as too great, and will take the decision not to bid for the project in question.

## Recommendation 7

*The WA Government should undertake an assessment of insurance as it relates to all stakeholders involved in the procurement of government infrastructure, with a particular focus on the understanding, costs and uptake of indemnity cover by professional services firms and builders.*

## Insurance amounts

In recent contracts, requirements for professional indemnity insurance and public liability insurance amounts are unreasonably high and bear little relationship to the risk profile of the project. This has the effect of increasing costs for consultants to bid for projects given those additional premiums have to be absorbed by the consultant (ie. they are rarely passed on to clients who are unwilling to fund such policies).

The Inquiry should refer to the Australian Procurement and Construction Council's *Professional Indemnity Insurance Guidelines in the Building and Construction Industry* for more information on this particular matter.

## Other consequences from inappropriate allocation of risk

Our experience is that on projects where all the risk is allocated to one party, there is less incentive for the

parties to work together to properly identify and effectively manage project risks. In particular, it allows one party to easily 'pass the buck' when they could have managed a risk, as contractually it is no longer their responsibility.

**When risk is more fairly allocated, a more collaborative approach is taken as each party has an interest in seeing the risks properly dealt with, and risks are allocated to those best placed to do something about them.**

This in turn leads to better project outcomes, including better and more efficient delivery of the deliverables, as well as reduced disputation and consequentially a better experience for all participants.

Best practice risk management sees the parties work together in identifying possible risks and solutions to manage them.

Less desirable practices are generally focused on one party offloading responsibility to another and considering the risk has been managed, when in actual fact it has not (and indeed may be allocated to a party unable to manage that risk).

This approach also focuses on what might happen in litigation after a risk eventuates, including seeking out the 'deep pockets' of certain firms or individuals, rather than preventing the risk from eventuating in the first place.

### **Deters Innovation**

While an innovative solution or design might not be appropriate for every piece of infrastructure, innovation nevertheless may offer a way of saving money or maximizing project outcomes and user experiences.

However, where the risk placed with a consultant is onerous, it will often result in them over-engineering their design, or increasing the conservatism of the design approach, to make certain that a risk does not eventuate, thus deterring innovation.

Similarly, onerous risk allocation could result in builders being more reluctant to offer alternatives and innovation.

### **Price Increases**

The Deloitte Access Economics report commissioned by Consult Australia, *The Economic Benefits of Better Procurement*, found that firms often respond to onerous

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risk by either pricing it into their bid, or deciding not to bid on a particular project which in turn drives up prices because of reduced competition. The report found that savings of about 5.4 per cent could be made through better risk sharing and other improved practices.

This is aside from the cost of lengthy negotiation and managing an onerous contract, or indeed the cost of disputation and litigation. A 2009 study<sup>7</sup> by the Cooperative Research Centre for Construction Innovation found the cost of disputation to be worth around \$7 billion in that year in Australia, adding around 6 per cent to the overall cost of work done.

While onerous risk allocation results in some firms pricing it in or declining to bid, a further unwanted consequence arises when, either knowingly or unknowingly, the risk is not priced. This puts more prudent businesses at a disadvantage and the successful under-bidder in jeopardy of loss or failure.

## Further Delays

Delays could be reduced by 7 per cent through better procurement, according to Consult Australia publication *The Economic Benefits of Better Procurement*. Onerous contracting is more likely to lead to disputation, as well as lengthier negotiations in the initial phase.

Should a risk be realised and a liability eventuate, an onerous contract means there will be less incentive for the parties to settle expeditiously instead of pursuing costly litigation.

## Inferior Project Outcomes

Successive reports have established that a greater investment of resources in the conceptualisation, scoping and design of a project will ultimately yield a better project outcome, and may even save money over the life of the project. Inappropriate risk allocation reduces the incentive for professional services firms to do this.

## Reputational Damage

Certain public sector agencies have over time developed a reputation for using onerous contracts and procurement processes. Accordingly, many private sector service providers are reluctant to tender for work with that agency, knowing that it will be less collaborative and a riskier job.

Ultimately, this should concern any agency seeking the best solutions to their projects, including the best possible designs.

## Viability

Reduced competition in the market will result in less choice, higher prices, and poorer value for money outcomes.

## Recommendation 8

*As part of a new WA Government Policy on Best Practice Procurement of Government Infrastructure, set clear guidelines for the allocation of project risk.*

## 5 | STANDARD CONTRACTS

Already a number of standard, fair contracts exist around Australia and have been used with great success by government agencies, including in Western Australia.

The use of standard, fair contracts negotiated between industry and government, with input from relevant stakeholders, reduces the need for costly legal review or negotiations and gives all parties the comfort of knowing that risk and reward is allocated fairly to avoid many of the negative outcomes described above.

While we acknowledge that standard contracts will not be appropriate on all projects (for example, unique major infrastructure projects), we strongly recommend that government agencies use standard contracts on an 'if not, why not' basis, whereby the public service is required to use them unless there is an appropriate reason not to do so that is explained to their industry partners and recorded publicly.

One other issue frequently encountered with the use of standard contracts, including from certain WA Government agencies is the attachment of special conditions. Where agencies do attach special conditions, they need to be aware that doing so undermines the benefit of using a standard contract, as otherwise-avoided further negotiation is often required like in the case of using a bespoke contract.

<sup>7</sup> Cooperative Research Centre for Construction Innovation, *Guide to Leading Practice for Dispute Avoidance and Resolution*, www.construction-innovation.info, 2009, p8

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Some standard contracts already in use with great success include:

- **AS4122-2010:** The Australian Standard contract for engagement of consultants in the construction sector was developed through Standards Australia, with the input of industry and government representatives.
- **AS4000-1997/AS2124-1992:** The Australian Standard for General Conditions of Contract used for engagement of building and construction firms was developed through Standards Australia, with the input of industry and government representatives.
- **The Commonwealth Suite of Contracts** for projects valued at up to \$200,000. This contract retains a fair allocation of liability, and leaves industry to determine the best insurance management process themselves.

There are also presently several similar state based standard agreements.

We believe that the WA Government and our industry would benefit greatly from the use of a standard contract for professional services, offered on an 'if not, why not' basis. AS4122-2010 and AS4000-1997/AS2124-1992 are considered the best standard agreements to use.

In those circumstances where public sector clients deem this agreement inappropriate, they should always be prepared to explain to their industry partners why that is the case, and should also understand that **unnecessarily onerous contracts will result in less desirable project outcomes, higher costs and less certainty.**

**Recommendation 9**

*The WA Government should adopt a policy of using Australian Standard 4122-2010 General Conditions of Contract for Consultants for all professional services, and Australian Standard AS4000-1997/AS2124-1992 General Conditions of Contract for building and construction, in the State on an 'if not why not' basis.*

## 6 | PROPORTIONATE LIABILITY

As this issue has broader policy implications, this submission will deal with 'proportionate liability' as a separate issue to the other risk related issues outlined above, together with a legislative solution.

In response to the insurance crisis of 2001, a package of reforms including proportionate liability legislation was enacted to replace the doctrine of 'joint and several' liability. Under this old regime, multiple parties may have combined to cause loss to a plaintiff, but any one of them could have been held fully liable, and be required to pay the full cost irrespective of their individual contribution to the loss.

Proportionate liability was introduced on the principle that any loss is divided among the parties according to their share of responsibility, as determined by a court.

Liability is therefore allocated to the parties according to who can manage the risk, rather than the party with the weakest defence capabilities, the deepest pockets, or away from the party(ies) with the greatest bargaining power.

While part of a national reform that sought to deliver a consistent approach, when enacting legislation was implemented at a state-level, a crucial difference emerged between the jurisdictions. While Queensland expressly prohibited the practice of not applying proportionate liability in a contract (known as 'contracting out'), the WA Civil Liability Act 2002 allowed for it (along with its sister legislation in New South Wales and Tasmania, while the legislation in other states is silent on the issue).

**This continued allowance under law to disproportionately allocate risk presents a significant issue to many professional services firms and contractors as it limits their ability and willingness to do business in Western Australia.**

Ensuring that proportionate liability is a feature of contracts will mean cheaper and readily available insurance for professionals and contractors, and better risk management.

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## Contracting out is a risk to the State

### Allowing contracting out of proportionate liability to continue presents as significant systemic risk to the procurement of government infrastructure in Western Australia.

The current wording of the Civil Liability Act 2002 supports a culture of poor risk management that will see Government:

- Pay higher fees for professional and construction services;
- Continue to fail to manage project risk appropriately;
- Be forcing many businesses to pay expensive additional insurance premiums, if available;
- Support reduced competition from firms unable to obtain or afford insurance;
- Support an environment where some firms proceed without insurance, at times unknowingly;
- Reinforce a culture of poor risk and contractor management, and of inappropriate risk offloading;
- Unnecessarily expose the state economy to future tightening in local and global insurance markets;

While Western Australia is currently presented with a robust global insurance market, insurance coverage for projects contracting out of proportionate liability has generally been very difficult to obtain.

Nevertheless, in recent years some policy extensions covering contracting out have been made available, but these are problematic for a few reasons:

- The additional premiums are expensive, at up to 25 per cent additional cost to already costly premiums<sup>8</sup>, and often don't make commercial sense.

- The policy extensions aren't universally available, and smaller businesses often are unable to obtain them.
- The policy extensions available now may not be available when the insurance market hardens. Thus, future claims made against current projects may not be insured, and often with little awareness that this is the case.
- A sizeable portion of our industry does not have insurance cover for contracting out of proportionate liability.

In relation to this last point, for example, the Deloitte Access Economics study, *The Economic Benefits of Better Procurement*, found only 20 per cent of professional services firms have cover for contracting out, while a further 36 per cent were unsure whether their policy covered contracting out.

A broader issue also exists in industry being unaware of contracting out of proportionate liability and its implications. The study also found that a large proportion (38 per cent) of the professional services industry was unsure whether they were contracting out of proportionate liability, given that its standard wording in contracts is often highly technical in nature.

## Additional negative impacts

In addition to the various impacts of onerous contracts described above, contracting out of proportionate liability has a number of additional negative impacts:

- **Lack of certainty regarding insurance cover.** Firms entering contracts where proportionate liability does not apply are placed in a situation where their insurer most likely will not respond to claims. Even where a policy extension has been obtained, that may not cover a liability that arises in the future (see above).
- **Lack of awareness.** Firms are often unaware that they are contracting out of proportionate liability, or what the implications of doing so are. This means they may be under the impression they have taken steps to protect their business and client against liabilities, when in fact they

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<sup>8</sup> Deloitte Access Economics, *op. cit.*

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are exposing themselves to potentially significant losses. If such a loss does eventuate, the business in question will only become aware of the implications once it is too late.

- **Undermines the original policy intent of reform.** The original intent of the proportionate liability reform was to ensure that professional indemnity insurance remained affordable and available for industries such as ours that rely heavily on it. At the time of the HIH collapse, around 30 of Consult Australia's largest member professional services firms were simply unable to obtain insurance.

Should insurance not be available on commercial terms, a significant negative impact will be felt, not just by clients of industries that rely on it, but also on the broader Western Australia economy.

- **Focus on litigation rather than managing risk or successful project completion.** Contracting out of proportionate liability is predicated on making litigation easier for a plaintiff by making 'deep pockets' available to them, rather than driving better project outcomes, including better managing risk and preventing a liability from occurring in the first place. Anecdotal evidence has shown that proportionate liability not only drives better project outcomes, but also creates a significant incentive for parties to settle any dispute ahead of litigation.

## WA needs to act alone, for now

In the past, there has been a concerted effort to achieve a uniform national position where each Australian jurisdiction's legislation consistently prohibits contracting out of proportionate liability. This position was supported by expert advice presented to the Standing Council on Law and Justice (SCLJ) (previously the Standing Committee of Attorneys General)<sup>9</sup>.

In October 2013, the Council released draft legislation to remove contracting out, although the draft contained loopholes that would have been used to bypass the reform. However, no legislative reform has been enacted.

Given the lack of impetus for a national legislative change, we strongly recommend that WA act to remove the ability to contract out of proportionate liability from its contracts and the underlying legislation. This will further support efforts to attract the professional services sector and contractors to do business in WA, and will also support small business, while furthering the original policy goals of proportionate liability.

To further understand proportionate liability and the October 2013 proposal, we recommend Consult Australia's factsheet on *Poor Risk Allocation and Proportionate Liability in Western Australia*, and the submission to the SCLJ consultation, included as **Appendix C & D** respectively.

### Recommendation 10

*The WA Government should immediately prohibit the contracting out of proportionate liability from all government contracts with professional services and building firms.*

### Recommendation 11

*The Civil Liability Act 2002 must be amended to prohibit the contracting out of proportionate liability for apportionable claims, notably through reform of Section 4A(1).*

<sup>9</sup> Horan, T., *Proportionate Liability: Towards National Consistency*, DLA Phillips Fox, September 2007; and Em Prof Davis, J L R,

*Proportionate Liability: Proposals to Achieve National Uniformity*, Australian National University, 2008.

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## PART III - QUALITY AND COST

### **7 | QUALITY OF PROJECT PLANNING**

Together with risk management, the quality of project documentation is the other major roadblock in the push for better procurement. When project documentation does not meet the required standard, it frequently becomes a major project risk in itself, leading to disputation, increased prices, or decisions for firms not to tender for certain projects.

Project documentation includes the scope of works, which sets out the client's requirement from the project. While the scoping of each project will vary on a case by case basis, there are several components that are generally common to all projects. They include:

- Outlining the broad objectives of the client to be realised through the project;
- Specific project requirements, such as functional outcomes or benchmarks to be met in meeting the broad objectives;
- Background information, including specific project risks; and
- Contractual method of delivering the project.

There are many paths taken by clients to develop an initial concept into a scope, although these processes aren't always clear to the various service providers who will then rely on that documentation. What is clear is that the best quality scopes have a greater level of input from a wide range of stakeholders (including the potential for service providers such as consultants and contractors), contain realistic timeframes and budgets, provide an appropriate amount of background detail, and tailor the procurement process (including risk and delivery method) to the circumstances of the project.

Indeed, the level of clarity in the scope should be a deliberate factor linked to the delivery model and appropriate risk allocation in order to encourage innovative solutions. On the other hand, **poor project scopes lead to confusion and wasted efforts by all parties, and a greater likelihood of disputes and litigation.**

The key problems with project documentation highlighted in our various procurement studies include the following areas:

#### **Unclear objectives and early engagement**

Unclear project objectives create a challenge for tenderers in putting a bid together, when they are not sure of what the client wants, which should be set out as a minimum inclusion in a scope. In some cases, scoping documents are used by clients to clarify what they want, when they are deliberately vague, in the hope that a consultant will challenge the information provided in terms of "you have asked for X, but don't you really want Y instead?" This issue creates significant risk for consultants, who respond by pricing that risk into their bids, not bidding for work, or submitting a non-conforming proposal.

The Deloitte Access Economics study found unclear project objectives to be one of the most commonly occurring problems with procurement, with 37 per cent of projects being affected by this issue. Furthermore, only 20 per cent of bidders presented with this issue continue their work without adding a price premium, deciding not to bid, or submitting a potentially non-conforming bid.

While the level of detail required in a scoping brief will vary by project, the converse argument can also be made in some cases; that leaving certain aspects of a project open might in turn encourage innovation by testing the creativity of bidders. What is an imperative is that any lesser degree of detail should be deliberate, and not simply a planning oversight.

A possible solution to this issue might be early engagement to get industry feedback on the proposed project, or even to engage a consultant to reverse-engineer a project brief, on the understanding that they are then unable to further tender for its work. Under this arrangement, they are able to test out a range of assumptions, and use their technical knowledge to flesh out project objectives before it goes to market.

#### **Inadequate or unverified background information**

Background information to a project is often included in project documentation, but it is common for public sector clients to refuse to verify any of that information, or provide inadequate information – requiring duplication and over-servicing by consultants and

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contractors participating in the tender process.

For example, this may include a geotechnical survey of land a building is to be built on, background financial data, or an environmental impact statement. As any inaccuracies in such information might mean a design is unusable, the accuracy of this information is vitally important. In each case, the refusal to allow bidders to rely on that information means that each bidder individually needs to duplicate that work.

The cost of verifying background information was found by the Deloitte Access Economics study to be \$41,800 per firm, per bid on average. Given that in many cases, designs are based on that background information, this is a gross inefficiency. Furthermore, a 2005 report published by the Queensland Division of Engineers Australia,<sup>10</sup>, found that between 60 per cent and 90 per cent of variations are due to poor documentation, with the ultimate cost to public sector clients totaling billions of dollars.

Government verifying brief information and even going so far as to hold the original provider of that information responsible for its accuracy could remove a major inefficiency of the procurement process.

This issue goes to a much broader challenge on how data relating to built environment projects in Western Australia is considered, held and utilised by government, industry and the public.

## Form-based scope development

A standardised, form-based approach to developing the scoping document may be problematic, as it runs the risk of developing the scoping document for the sake of producing the document, rather than meeting project needs.

The best scopes are developed specifically for a particular project, and acknowledge project requirements and risks unique to that site, the relevant set of stakeholders, and the desired final outcome. Our industry reports having been presented with scoping documents that in some cases weren't even updated from their previous use for a similar project, such as a corridor preservation or traffic study.

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<sup>10</sup> Engineers Australia Queensland Division and Queensland Construction Industry Forum, *Getting It Right – The First Time*, www.qcif.com.au, 2005

## Inclusion of unnecessary items

Linked to the previous frustration is the inclusion in the scope of items that aren't really required. For example, certain skills may be listed as a requirement from firms tendering for a particular job, or other requirements for the project may be prescribed when they are not necessary.

Ultimately, demanding that a successful bidder meets certain unnecessary requirements or brings unnecessary characteristics will deter certain firms from competing for tenders, and will drive up the cost on the part of other firms. In both instances, needless additional costs are incurred and inefficiencies result, while at the same time stifling the potential for innovation on that project.

## Improving project scoping

Our members have regularly reported receiving project briefs that appear not to have been reviewed for accuracy or where additional information released has been difficult to access. Some examples reported by members that reflect each of the issues canvassed here include<sup>11</sup>:

- The re-issue by the agency of an entire project brief, but without track changes, making it extremely difficult and time consuming for tenderers to ascertain where the changes have been made and the implications for a tender already underway;
- Project briefs that do not correctly refer to known industry standards;
- Project briefs in a 'state of flux' evolving throughout the tender period with additional information catering to changing client demands;
- Tender advertisements referring to published information that is not available online;
- Addenda being issued, sometimes the day before a tender deadline, with no time extension;
- References to parts of a project that are not actually relevant to the project being tendered;

<sup>11</sup> Some examples drawn from: Consult Australia, *QLD Government Procurement Review: Response to issues Paper*, www.consultaustralia.com.au, November 2012

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- Project briefs that refer to construction phase services for projects where there is no need for such services; and
- Increased demands for building information modelling (BIM) without associated increases in time to prepare such requirements.

In the circumstances cited above, quality assurance has not been correctly administered and, in part, the costs of quality assurance have effectively been passed to the consultant where they choose to engage with the tender and raise issues of concern.

The time and costs associated with this process are substantial, and will either detract from resources spent on the preparation of the tender, or increase costs to the client and consultant alike.

Ultimately however, of greater concern to the taxpayer are the ongoing unmanaged risks to the Government that arise in the absence of robust quality assurance.

## Investing more in scoping

Better quality project briefs will make it easier for consultants and others in the design phase to conceptualise a project. Multiple studies have shown that poor quality project briefs are a major source of inefficiencies in building infrastructure. This is highlighted in the *Western Australian Auditor General, Major Capital Projects Report 12 of October 2012*, which states that 'Approximately 90 per cent (\$2.953 billion) of the cost variance for projects occurred during the evaluation phase of the project when the project business case was developed and the project scope and costs were more accurately defined.'

Reallocating procurement resources towards better specification of project objectives will ultimately save a project money, as potential problems are resolved before it's too late.

### Recommendation 12

*Pre-procurement consultation, including early project definition planning and business case development, should be undertaken, where appropriate, to ensure project objectives are sufficiently clear and to support innovation before any tender process begins.*

## 8 | SUPPORTING INNOVATION

Innovation has the potential to save a client money, mitigate risk, or deliver a better project outcome. Most significantly, innovation in the procurement of government infrastructure is key to allowing Western Australia to maintain its edge as a preferred place to do business and to delivering the best value to taxpayers.

Public sector agencies are historically risk averse, which means they might not be as open to innovative solutions as they should be. The *Economic benefits of better procurement practices* report found that public sector agencies were generally reluctant to allow innovative solutions before a project commenced, with the major reasons cited being probity concerns, fears of negative budget impacts and delivery mechanism.

The Deloitte Access Economics report, together with *Better Buying, Better Outcomes* canvassed some ideas for encouraging innovation to the benefit of public sector clients.

One element of doing so in many cases will be to accept the potential for failure, either by quarantining a portion of funds for innovative projects, or to work collaboratively with the consultant to manage the risks in play. The scope of works, risk management process, contract terms and conditions, or delivery model will determine for a firm planning a bid, whether an innovative solution is suited to that project or not. A scope that isn't overly prescriptive in terms of the definition of the project outcome (as distinct from project aims) will encourage innovation, as will delivery models that share risk and support collaboration.

Clients who recognise the potential cost-saving benefits of innovation and seek them out, should be aware of this when developing their project documentation and delivery model. Industry recognises that these solutions won't always be possible, and also that innovation isn't always appropriate for every project.

Other suggestions include better early engagement of agencies with consultants and contractors, either as an early market sounding process or during the bidding process, and updating market led proposal mechanisms to account for the needs of consulting firms.

In the case of early engagement, our industry reports that this only occurs in around half of all projects, while

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the major challenge with market led proposals is that developing such a proposal is a costly exercise for consultants to undertake without the comfort of knowing the project will be approved. Currently, the Victorian Government is investigating mechanisms to support consultants in undertaking this work, and we would recommend that the WA Government follow suit.<sup>12</sup>

To ensure that innovation is recognised for the benefits it brings, rather than being feared as a form of gold plating assets, it is important that clients select the appropriate projects to try innovative solutions. For example, mature technology might be more appropriate for a large infrastructure project, such as a highway or hospital, while novel projects may emerge more innovative solutions.

## Recommendation 13

*The WA Government should establish and oversee a strategic Procurement Innovation Fund to allow them to work with specific agencies to trial more innovative ways of procuring government infrastructure without impacting negatively on project budgets and allowing for savings to be paid back into the fund.*

## 9 | COST OF BIDDING FOR WORK

Our industry frequently asserts that bidding for work is expensive, often to the point of being prohibitive. While the tender phase of a project is important for clients to evaluate the range of project solutions on offer, and use competitive pressures to achieve the best value for money, the nature of bid processes in Western Australia could be improved to save industry money, and in turn reduce the costs that ultimately are passed back to their clients and the taxpayer.

As well as the cost of the time spent putting a bid together, other expenses might include the cost of the intellectual property included as a possible solution to the brief, or the resources required to test any background information. Red tape type administrative hurdles are also fairly common through the tender process, as bidders are asked the same question multiple times through the different stages of the one tender, which can be costly to duplicate.

In other situations, bid documentation is required to address the bidder's compliance with a range of competencies, which ultimately will play little role in determining the final awarding of the contract. Meanwhile, some consultants report having been subject to tender processes that required them to "almost do the whole job" in the bid phase, but without the reward of a fee in return.

## Appropriate client behaviour

Certain client behaviours further drive these expenses. For example, shortlisting has the potential to help save costs, but this purpose is defeated if too many bidders are shortlisted, as they continue to accumulate costs associated with their bid that ultimately have to be met (e.g. recouped through other tenders for which they are successful).

On other occasions, consultants and contractors report being asked questions completely irrelevant to the work at hand, as the client is using a form approach to procurement, and answering those questions has a cost attached as well. Other factors, such as the requirement for bids to be fully compliant, undue complexity of the tender process, or lack of clarity surrounding project risk also impact on the cost of tendering.

Many in our industry recognise that the cost of bidding for work is the price of doing business, but ask that clients respect and consider the cost imposed on businesses through their approaches. For example, this means not calling for bids on projects simply to make up numbers, when there's already a preferred supplier, including at the second stage of a two stage process. The adage that a 'quick no' is preferable to a slow one is especially true in our industry.

Client recognition of the cost of tendering in and of itself is at the core of any solution to this issue. Clients rely on a viable consulting and contracting industry, and short term costs to the industry will have a longer term impact. By understanding the various costs that go into preparing a bid for work, clients can reduce the cost to industry by better focusing the questions they ask, and reducing duplication through the bid process for the one job.

<sup>12</sup> Department of Treasury and Finance (Victoria), *Market-led Proposals Guideline*, www.dtf.vic.gov.au, November 2015

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The selection process could also be structured to prevent keeping bids alive when they have no realistic prospect of success, while the issue of reimbursing unsuccessful bids in return for the use of (part or all of) their intellectual property is also worth considering.

## Pre-qualification schemes are useful

While government clients rightly ask industry to demonstrate that they meet certain competencies, a centralised database or even a pre-qualification scheme would be preferable to bidders filling out the same forms on multiple occasions. In their report on public infrastructure, the Productivity Commission recognised<sup>13</sup> that the bulk of bid content was comprised of this type of paperwork, rather than proposals relating to the project at hand, that could usefully differentiate the bidding firms.

Any move to reduce the need for this compliance activity represents a significant opportunity for government to save on the cost of bidding, while also supporting industry.

## Quantifying the cost of bidding

We would also like to draw the Inquiry's attention to previous Consult Australia reports<sup>14</sup>, which have cited the 1996 study by the Office of Building Asset and Building Policy in Victoria, which compiled some examples of bidding costs, including:

- For a \$320,000 public facility, one tender submission by an architectural consultant cost \$9,000 to prepare. 102 tenders were submitted. If each tender cost the same amount, potentially \$918,000 would have been spent on the preparation of submissions by tenderers and the total cost of tendering equated to almost three times the project value;
- For another public facility, the client found that tender bid prices were too high so made minor changes to the tender documents and re-tendered the projects. The client was effectively bid-shopping, but this required the tenderers to put in extra work.

- For a \$5-6million project a consultant spent \$100,000 to prepare a bid. The successful bid was awarded a contract worth \$180,000, meaning that the consultant only received \$80,000 for the project and the rest covered their tender costs. The unsuccessful tenderers did not recoup any costs.

Our collective members have regularly reported that that these figures remain relevant today and are not by any means unusual.

## Streamline compliance processes

The vast majority of tender documentation is not used to differentiate bidders, but to ask bidders to verify that they meet a range of competencies that might be relevant to the project at hand.

This practice is a major driver behind the high cost of bidding for work, which could be reduced through streamlined compliance processes, perhaps in the form of a central register of competencies held by various firms and individuals, in line with pre-qualification requirements.

### Recommendation 14

*As part of a new WA Government policy on Best Practice Procurement of Government Infrastructure, recognise the time, effort and costs assumed by industry in the preparation of tender documents and seek to reduce these wherever possible, and to provide compensation where appropriate to encourage competitiveness, innovation and industry sustainability.*

<sup>13</sup> Productivity Commission, Public Infrastructure, Inquiry Report No. 71, Canberra, 2014

<sup>14</sup> See [www.consultaustralia.com.au/Home/Advocacy](http://www.consultaustralia.com.au/Home/Advocacy)

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## **PART IV - EVALUATION AND STAGING**

### **10 | BETTER DECISION MAKING**

One aspect of procurement often overlooked when policy makers consider areas for possible reform is the quality and nature of decision making.

The type of decisions relating to the procurement of government infrastructure generally fit into a small number of categories:

- Decisions around which project to undertake;
- Decisions around project specifications; and
- Decisions around selecting the winning bid(s) to work on the project.

While the first of these decisions is generally beyond the scope of this Inquiry, nevertheless we would like to take the opportunity to highlight the importance of independent advice to government based on expert opinion to optimise the quality of these decisions.

In terms of decisions around project specifications, some important and competing considerations will determine what the agency responsible for the project will select.

Collectively our members have welcomed the prospect that Infrastructure WA will soon be established as an independent agency to make recommendations to government about a longer term, 20 plus year, infrastructure plan for the State. Our members collectively call for any such authority be not only established in statute, but also is structured in a way that provides an even mix of both government and industry representatives who are experts within the infrastructure, planning, design, building and finance sectors so that it is best placed to plan for our State's future.

#### **Deadlines and budgets**

As the system of infrastructure development currently operates, there is great focus placed on time and budget considerations. These are often used as indicators of project success by Cabinet, individual

ministers, and the public service, and indeed are important factors in a project's success. However, they should not be pursued at the expense of the project meeting its original aims.

If a project fails to meet the original aims, it will not be a good use of taxpayers' money, and will likely require costly upgrades at an earlier time than might otherwise have been required.

Furthermore, the discussion around whether to focus on cost or value set out below with regard to bid decisions, also applies to project specifications overall.

#### **Whole of life considerations**

Consideration of 'whole of life' factors is an important element that should be considered in any decisions around project specifications. Often, infrastructure is built to specifications that allow it to be built, but without sufficient consideration for future demand and alternative uses (known as 'future proofing'), and in turn reaching capacity or the end of its useful life earlier than might otherwise occur.

In contrast to infrastructure procurement today, when the Sydney Harbour Bridge was opened in 1932 it had the capacity to allow every car in the state to drive it, simultaneously provided rail and tram access, with the capacity to also accommodate a future Northern Beaches Railway.

In other instances, the 'whole of life' specifications may not refer to capacity of infrastructure, but to the cost of operating, maintaining, and even decommissioning that infrastructure. It is important that such elements are factored into any decision making in regards to the procurement of government infrastructure.

We acknowledge increased future proofing of infrastructure comes at an additional upfront cost. That additional price tag in turn will have its own opportunity cost, in that it cannot be spent on other projects, or may lead to a project being rejected at the initial planning stage.

Nevertheless, coming back later to upgrade existing infrastructure will invariably cost significantly more than if the project had been built to its optimal specification in the first instance.

Ultimately, these competing considerations need to at least be considered by government, if not reconciled.

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Considering future use of an item of infrastructure, and whether it is worth constructing that infrastructure to a greater specification to save money over the long term is an important decision that must be made.

## Recommendation 15

*As part of a new WA Government policy on Best Practice Procurement of Government Infrastructure, recognise the need to consider 'whole of life' costs that ensure appropriate consideration for future demand, later stage expansion, alternative uses, maintenance, operational and decommissioning costs.*

## Measuring risk

Making decisions around project specifications often relies on understanding the risks associated with the project, and how to overcome those risks. In our experience, there is a strong bias amongst public sector clients towards regarding their project as riskier than it is.

This in turn will require service providers to unnecessarily carry more insurance than is needed (with the additional premiums being passed back to the client through a higher fee), and will also have an impact on project specifications.

The work of the Australasian Procurement and Construction Council (APCC) in particular should be considered in addressing how the public service currently approaches, and should approach, managing risk.

## Bid selection: cost v value

The third category of decision making mentioned above is the decision around which bidder to select, and the rationale for doing so. One of the major issues faced here is whether a government agency should prioritise cost or value in selecting the winning bid.

Whilst the Association of Consulting Architects *Procuring Architectural Services, An Industry Discussion Paper* of April 2017<sup>15</sup> is worth further consideration by the Inquiry, collectively our members

have advocated for some time that the best outcome is always going to be achieved by selecting **best value bids, rather than simply the lowest cost.**

Selecting just the cheapest bid invariably takes a short-term approach to the planning and procurement of government infrastructure, and potentially creates risks where the lower priced bid has saved money by ignoring or being unaware of certain risks or other factors related to the project.

Often, a cheaper bid will end up costing more than a rival bid that was more expensive at the initial stage, as variations are added to the project, which steadily increase its cost.

Unusually low bids, as different to just low bids, have the potential to cost both the WA Government and Industry more in the long term by undermining both the delivery and maintenance of major infrastructure projects within the State. The practice of submitting unusually low bids has a direct impact on the long-term sustainability of professional services and builders within the state and should be actively discouraged by the WA Government.

From a client's perspective, the public service should understand their projects and their associated risks, and have an idea of the amount that an optimal bid will be made at. In turn, they should ask questions of any bid that deviates too far from this amount.

Bids that come in too low will likely have not accounted for some risks, and bids that come in too expensive may have a less efficient solution to managing those risks. While some clients already eliminate the cheapest bids from consideration, measuring bids against an optimal cost will support more informed decision making.

Suggestions as to the process of finding the best value bid are also worth consideration. Such as the use of a 'two envelope' system: separating price and non-price information, evaluating each bid according to their ability to perform the work, before then moving to price considerations for those bids with the ability to perform the required tasks.

A number of our members report an undue emphasis on price in tender selection rather than capacity to deliver, their experience, or value for money.

<sup>15</sup> Association of Consulting Architects, *Procuring Architectural Services, An Industry Discussion Paper*, www.aca.org.au, April 2017

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Assessment criteria focus too much on requiring detailed information on costings and hours budgeted, rather than a qualitative assessment of deliverables. This is understandable, given that the quality of their output won't always be easy to assess or benchmark, while the level of their fee will be.

Tied in with transparent selection criteria and weightings is the idea that unsuccessful bids should get feedback. We acknowledge that this may create an additional administrative burden for agencies in the short term, but it has the potential to lead to savings over the longer term by improving accountability and probity, and in turn will drive improved decision making.

**Recommendation 16**

*The WA Government should implement a 'two envelope' approach to tender consideration, allowing for the expertise and capacity of professional services firms to be considered separately from the tender price and independent price assessment, if undertaken.*

**Recommendation 18**

*The WA Government should establish a practice of setting and disclosing selection criteria and weightings for all tenders, with this information centrally collated by the WA Government for future data analysis.*

**Recommendation 17**

*The WA Government should implement an agency wide 'unusually low bids' policy and ensure that such a policy is used effectively to discourage such practices from occurring.*

**Recommendation 19**

*Standard practice in Western Australia should be firms involved in unsuccessful bids are provided with detailed feedback when requested.*

## Clarity about selection criteria

Service providers in the built environment sector regularly report frustration at the lack of clarity around bid selection criteria. In *Better Buying, Better Outcomes*, our industry reported that clients weren't always open or able to tell them about the framework for selection or the selection criteria, including the relative weighting of each item throughout the tender phase.

## Non-conforming bids

One particular challenge is how public sector agencies address non-conforming bids (those that do not align with requirements). Too often non-conforming bids are excluded from a tender process automatically, even when their non-conformity raises an important issue(s) the client should address. In particular, some members have reported experiencing problems when bids were submitted through portals, which have no flexibility to accept a non-conforming bid.

On some occasions, they reported that the weightings changed after bids were submitted, which left some firms at a disadvantage.

Where the public sector client brief includes an erroneous scope item, at times some of our members are challenged as to whether they should second guess what they actually wanted, or respond to the brief with the error factored in.

These issues have the potential to waste the time and resources putting together a bid that didn't address the right issues, and or focused on less important aspects of the client's decisions.

Clearly a better project outcome will eventuate when a non-conforming bid is considered that addresses the actual issue, but it does raise probity concerns towards other bidders who weren't aware they could do this.

Greater transparency around the selection criteria in the tender process is frequently requested as a means to ensure that firms only bid for work appropriate to them, and that they have proper awareness of what to address in their bids.

Apart from improving the quality of project briefs, the solution to this issue lies in allowing bidders to challenge the assumptions in a brief where appropriate, and to

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address the associated probity concerns by adopting a policy making it clear that this is allowed.

While the 2014 *Scope for Improvement* Report identified the automatic rejection of non-conforming bids as a source of rising costs and inefficiency<sup>16</sup>, this practice also has the potential to bypass a quality control element of the tender process. Although some guidelines would be required, considering non-conforming bids under certain circumstances could allow for errors in the scope to be identified, or for more innovative solutions to come forward that might save clients money through the procurement process.

## Recommendation 20

*As part of a new WA Government Policy on Best Practice Procurement of Government Infrastructure, provide guidance on when it is appropriate to consider non-confirming bids and what should occur when issues or problems are found with the tender process or project brief.*

## **PART V - MONITORING, RESEARCH AND REPORTING**

### **11 | UNDERLYING CAUSES**

This submission thus far has looked at a range of procurement issues that present opportunities for improvement. However, any such discussion also needs to look at the underlying drivers of less desirable procurement practices.

In our experience, these underlying issues are significant, and without addressing them, any changes to procurement policy will be limited in their ability to achieve positive reform.

#### **Procurement skills**

As part of the decline in government procurement expertise over the last few decades, collectively our organisations have seen a critical ongoing shortage of

staff with relevant contemporary procurement skills across multiple levels in government. Where previously in-house professionals within Departments may have undertaken a project, or done design work internally, now private sector providers are contracted to do that work. A natural consequence is that certain skills which existed within an agency are now less prevalent.

An erosion in the contemporary skills base of the public sector means that the standard of procurement and value for money outcomes are reduced while some responsibility for procurement has shifted to contractors. This is demonstrated in our members' ongoing concerns in relation to:

- Poor quality tender and project scope documentation;
- Poor risk management; and
- Poor quality contractual terms and conditions and undue reliance of external legal advice.

These are evident throughout the Western Australia public service, indicating a possible systemic procurement skills shortage at all levels.

This issue is increasingly of concern nationally and not just isolated to WA. It is incumbent upon government to take some responsibility for public sector procurement skills, as a small investment that could yield significant returns over the long term.

The Australasian Procurement and Construction Council (APCC) as part of their guide, *Developing the Government Procurement Professional* acknowledge that:

*"Until now, procurement professionalism in Australia has not been clearly recognised or defined. Public procurement too often is undertaken without professional support which results in sub-optimal value for money decisions and unnecessary high prices being paid for goods and services."<sup>17</sup>*

Collectively we believe that a concerted, whole of government focus on procurement skills would benefit those agencies responsible for procuring consulting and contracting services. To this end, the concept of a *Centre for Procurement Excellence*, tasked with skills

<sup>16</sup> Ashurst Australia, *op. cit.*, p43

<sup>17</sup> Australian Procurement and Construction Council, *Developing the Government Procurement Profession*, www.apcc.gov.au, 2006, p3

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training and development for public sector procurement professionals, and sharing best practice between agencies, could be of benefit. This would include training for new procurement officers, as well as ongoing training for those already in procurement roles.

The creation of this concept is not without precedent. Already, the United Kingdom Government has created a *Commissioning Academy* that has broadly the same mandate in terms of sharing best practice and improving procurement skills. Given the reluctance of government to create new agencies, a *Centre for Procurement Excellence* could easily sit within an existing agency established to support the development of infrastructure or procurement skills.

While ideally this should be a national body, its function is sufficiently important that Western Australia could act alone in the immediate term in the context of a broader assessment into government procurement within the State.

## Recommendation 21

*The WA Government should undertake an assessment of insurance, contract and risk literacy within the public service, using this to facilitate appropriate training in conjunction with relevant professional and industry associations.*

## Public sector culture

The culture in which procurement decisions are made is also a vital driver of less desirable procurement practices. In our experience, the Western Australia public service (as elsewhere) has a tendency to be overwhelmingly conservative in its approach to procurement. While at one level, this is appropriate for those guarding the public's interests, including the appropriate spending of their taxes, it is also an approach that can be problematic when not properly applied. In particular, it is an approach that fails to take up new opportunities to do things better.

There is a common presumption within the public service that because something has 'worked well' in the past, that it will work well in the future. When suggesting procurement reform, one of our main challenges has been overcoming institutional inertia – asking agencies, and key procurement officials within them, to do things

differently without an obvious project failure as justification for change.

This approach inherently makes government slow to adapt to new ways of doing things. Clients who only ever procure infrastructure a particular way will be unaware that they've paid too much, as the alternative methods that would achieve a cheaper price have never been attempted. Indeed, project success may occur in spite of poor procurement, provided that project risks do not eventuate.

In the course of the *Better Buying, Better Outcomes* study, a senior public servant offered the observation that, "in the public service, you're rewarded for not stuffing up, rather than for getting it right." In other words, the focus is on not making mistakes and on avoiding liability for any mistakes that are made, rather than achieving the best possible outcomes from a project.

This culture is driven by a series of accountability measures connected with our political system, placing the entire apparatus of government on the defensive. For example, instead of looking for better ways to do things when ministers or their staff involve themselves in procurement issues, it's generally in response to claims of something having not worked, rather than to proactively drive positive change.

Generally, our organisations experience has been that ministers and the leadership of public sector agencies say the right things and are committed to best practice procurement.

The challenge is that individual contract managers are generally the people responsible for managing the procurement practices around a specific project, and are also the people most acutely aware of the ramifications for them if things go wrong.

The culture described above is most acutely felt by them, and they have little incentive to try new things. Indeed, through the public-sector culture they are actively discouraged from attempting newer and better ways of procuring infrastructure, and are given little in the way of protection to specifically encourage them to do so.

The outcome of this culture is that opportunities for innovation and achieving better outcomes are lost, and approaches to risk and liability are reflexive rather than proactive. A better approach would re-focus relevant

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personnel towards achieving successful project outcomes, rather than avoiding mistakes, and providing a level of protection for officials doing things differently than to how they may have been done before. This may be achieved through a whole client agency buying in to procurement outcomes, including its leadership.

## Recommendation 22

*That care is taken to understanding and address the public-sector culture as a key component to implementing existing and future reforms in the procurement of government infrastructure in Western Australia.*

## Accountability of Agency Heads

The suggestion has been made that procurement performance indicators should be used for agency CEOs and Department Secretaries to overcome the problem that many agency heads say the right things about procurement to industry, but are not backed up by the actions of individual project managers.

This would ultimately serve to improve procurement by offering a significant incentive for agency heads to offer protection or encouragement to individual procurement managers to try new and better ways of doing things.

## Recommendation 23

*Incorporate procurement performance indicators into the measurement of WA Government department/agency/GTE heads and senior management.*

## 12 | CONCLUSION

The decision was made to collectively **focus solely on Item 3 of the Terms of Reference to this Inquiry, namely the 'adequacy of their procurement processes'**, so as to ensure our respective organisations and members:

1. Do not get caught up in any potential politicisation of particular projects; and
2. Can collectively highlight key areas of concern to do with past and current government

procurement practices that continue to adversely impact our members.

And whilst it is noted that Western Australia currently has an overall positive culture in the procurement of government infrastructure, there still remains a particularly important need to address poor risk management practices by prohibiting the contracting out of proportionate liability, a need for greater consistency in contracts, and the need to address procurement literacy within the public service.

We are collectively aware and hopeful that any policy reforms that arise from this inquiry have the potential to dramatically assist our industry's operations, whilst also achieving better infrastructure and value for money outcomes for the people of Western Australia.

Consult Australia, Association of Consulting Architects, Australian Institute of Architects and Master Builders Association of Western Australia would like to thank the Inquiry for the opportunity to make our submission and comment on these important issues.

**We would welcome any opportunity to further discuss the issues raised in this submission and are all happy to appear publicly before the Inquiry if there is a need to do so.** To do so, please feel free to contact:

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